BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

I. An important point of appellate practice is presented.

The decrees entered in the District Court gave to the petitioner recovery on account of both bonds and coupons which its predecessor had acquired with its own moneys. The District Judge ruled that no prior notice was required to be given by the petitioner's predecessor in order for the securities thus obtained by it to participate in the reorganization. But he further went on and ruled in the case of the bonds as distinct from the coupons that notice had been given through the sending of the documents designated as resale authorities. He had before him a large number of these documents which were admitted as exhibits in the District Court and characterized them as "clearly indicating an intention to purchase" (Rec. p. 54).

The Circuit Court of Appeals held the judge's ruling that no notice was necessary was wrong and that notice must have been given. That ruling left the question of participation by the bonds dependent upon the effect to be accorded to the resale authorities. The Circuit Court of Appeals held that the use of them did not satisfy the requirement of notice.

The record was made up in conformity with Rule 75 of the new Federal Rules. The parties entered into stipulations, each of which stated:

> "It is stipulated and agreed by and between the parties in the above-entitled case that the record on appeal shall consist of:"

after which some eighteen documents were listed (Rec. pp. 60 and 103). The resale authorities referred to above were not the only exhibits introduced in the District Court. Certain of the other exhibits were sent up to the Circuit Court

of Appeals physically with the record. In each case the District Judge entered an order providing:

> "It is ordered, adjudged and decreed that the clerk transmit with the record on appeal the following original exhibits to be kept with the record on appeal for inspection by the Circuit Court of Appeals" (Rec. pp. 61, 101).

These orders were entered by the consent of the parties.

The resale authorities, which, in the District Court, had been designated as Exhibits 1a through 52a, inclusive, were not listed in either stipulation as to the contents of the record, were not referred to in either order for transmission of the exhibits, and were not in fact transmitted by the Clerk of the District Court to the Circuit Court of Appeals, with the printed record on appeal.

Nevertheless the Circuit Court of Appeals, in reaching its conclusion that the resale authorities did not satisfy the requirement of notice which it had laid down, obtained the exhibits from the Clerk of the District Court, considered them, and in its opinion referred to their terms (see Rec. p. 114). This was all done after the conclusion of the oral arguments and without any prior notice to the petitioner of what was being done. After the opinion was announced the petitioner moved for a rehearing and specified as one of the grounds therefor the inspection of the resale authorities thus made. The motion was denied and in consequence the petitioner has never been accorded the opportunity, which it still desires, to argue the sufficiency of the resale authorities as constituting notice by the petitioner's predecessor.*

*This argument was made successfully in the District Court. The judge stated in his opinion: "The additional fact that the Mortgage Co., in each case, took a re-sale order from the customer, *clearly indicating an intention to purchase*, is significant. These orders were notice to the customers of this intention" (Rec. p. 54, emphasis supplied).

The provisions of Rule 75 are clear and detailed and are designed to make sure that the record on appeal shall be the one on which the appeal shall be determined. It is provided in subparagraph (g) of the rule:

> "The matter so certified and transmitted constitutes the record on appeal."

The obvious intention is that the Circuit Court of Appeals should decide the case on the matter contained in the record on appeal and upon nothing else. This is but a carrying out of the well-established rule of appellate practice.

See *Fitzgerald* v. *Evans,* 49 Fed. 426 (C.C.A. 8).
Lydiard-Peterson Co. v. *Woodman,* 205 Fed. 900 (C.C.A. 8).
Krauss Bros. Lumber Co. v. *Mellon,* 18 F. (2d) 369 (C.C.A. 5).

Cf. *Chisholm-Ryder Co.* v. *Buck,* 65 F. (2d) 735 (C.C.A. 4):

In that case the point presented was whether the appellate court could take an exhibit not offered at the trial. The following language, however, is illuminating:

> "Ever since the system of equity jurisdiction was established, it has been the settled practice that an appellate court cannot look beyond the record before it to influence its judgment . . ." (page 737).

Likewise it has been held where some substantial matter is left out of the record it is ground not for dismissal of the appeal but for affirmance of the decree appealed from.

Bank of Eureka v. *Partington,* 91 F. (2d) 587 (C.C.A. 9).

The necessity for such a rule is obvious, since arguments and briefs can scarcely be kept within any reasonable

bounds if counsel must anticipate that the court will consider documents or other evidence not contained in the record on appeal.

Had the respondents desired to argue that the resale authorities could not satisfy any requirement of notice by reason of their terms, it was open to them to have them included in the record on appeal. They did not do so. In that situation the petitioner reasonably felt justified in giving no consideration to the language of the documents and in relying upon the finding made by the District Judge with reference to them. The action of the Circuit Court of Appeals in deciding the cases as far as the bonds were concerned on the basis of an inspection of these documents has resulted in depriving the petitioner of the opportunity to argue the sufficiency of the resale authorities, an argument which it most certainly would have advanced had counsel supposed that the point was open. This action of the Circuit Court of Appeals, we submit, constituted such a departure from the accepted and usual course of judicial proceedings as to merit review by this Court.

Our argument on this point is not that under no circumstances could the Circuit Court of Appeals consider the exhibits in question. If the Circuit Court of Appeals felt that it had an incomplete record by reason of the omission of these exhibits, Rule 75(h) provides a simple method for supplying the lack, but it does not justify the denial of an opportunity to argue, which resulted from the action taken by the Circuit Court of Appeals in this case.

II. An important point of law concerning dealings with corporate securities is presented in these cases.

The basic question involved in the present litigation is not one which is of importance solely to the parties to this action but has broad implications to all those who are

owners or connected with the flotation of corporate securities, and as such merits definitive adjudication by this Court. In the previously decided cases on this subject the tendency has been to require a choice between a "purchase" and a "payment." Petitioner submits that this does not represent a true analysis of the situation. In fact, the use of the terms "purchase" and "payment" introduces into the case semantic difficulties of the worst kind.

The basic situation involves, as here, the acquisition by a paying agent under a corporate indenture of bonds and coupons at or after their respective maturities. The indenture provides that obligations not paid by the issuer may be acquired by the paying agent for its own account and when so acquired may stand on an equal footing with other outstanding obligations secured by the same indenture. The question is, then, whether a paying agent who acquires matured bonds and coupons pursuant to such indenture provisions with affirmative intent to keep them alive as valid and outstanding obligations of the issuer with rights in the mortgage security equal to other bonds and coupons in the hands of the public is to have his expectation confirmed. Or is he, because he gave no notice of his intent, to be deprived of the parity which he in good faith on the strength of the indenture provision believed to be his due, and as a consequence forced to lose his money? This loss would be forced by the implication into the indenture of a requirement that he must give notice at the time of his acquisition of the securities that he proposed to claim a share in the mortgage security upon a parity with other bond and coupon holders.

Leaving aside the words "payment" and "purchase," neither of which aptly describes the situation, we are left with the simple question of whether or not the *method* of and the circumstances surrounding the paying agent's acquisition of matured bonds and coupons are such as to war-

rant denying him parity. No paying agent under the circumstances of this or any similar case would spend his funds to acquire mortgage bonds and coupons and so finance a default if he knew that the bonds and coupons so acquired would be deferred to the remaining ones in the hands of the public. Organizations placed in positions similar to that in which the American Bond & Mortgage Company found itself in the present case are entitled to a definite assurance as to whether or not they must give notice of their intention to claim parity for matured bonds and coupons which they acquire, and if notice is required, what sort of notice is sufficient. Such a definite assurance can be found, under the present conflicting state of the authorities, only in a pronouncement by this Court.

Where there is fraud or overreaching, of course parity will be denied. There was none in the present case. The Circuit Court of Appeals suggested no impropriety in the action of the American Bond & Mortgage Company. The furthest it went was to suggest that, if no requirement of notice of purchase was to be implied into the indenture, a situation would exist in which fraud might flourish (see Rec. pp. 112, 113). Unhappily, fraud may flourish in almost any situation. The question which we urge this Court to consider is whether this particular situation is one so susceptible to fraudulent practice that a party who has advanced large sums in entire good faith in reliance on indenture provisions which a District Judge has found could have no meaning unless they authorized what was done must forfeit them lest later some knave use its example for fraudulent purposes.

Until now the leading case on this question has been the decision of this Court in *Ketchum* v. *Duncan*, 96 U.S. 659, *supra*, but the decision of the Circuit Court of Appeals herein does not give proper effect to this Court's holding in that case. Mr. Justice Strong, speaking for the court, held

that intention was as much a requirement of a payment as it was of a sale. He said, at page 662:

> "It is as difficult to see how there can be a payment and extinguishment thereby of a debt without any intention to pay as it is to see how there can be a sale without an intention to sell."

The District Judge made no finding of the existence of an intention to pay on the part of the American Bond & Mortgage Company. On the contrary, he specifically found an intention not to pay but to purchase (Rec. p. 50). This finding was in no way disturbed by the Circuit Court of Appeals, but neither did that court give any effect to it. On the contrary, it wholly disregarded it. It is submitted, therefore, that the conclusion of the Circuit Court of Appeals that as a matter of law the acquisition of bonds and coupons by the American Bond & Mortgage Company was a payment, *i.e.*, was such a transaction as to prevent the securities acquired therein from being granted parity, did not give proper effect to so much of the decision of *Ketchum* v. *Duncan, supra,* as makes an affirmative intention by the paying agent a condition precedent to payment, with consequent subordination of matured bonds and coupons in his hands.*

Not only does the decision of the Circuit Court of Appeals in the present case fail to give proper effect to *Ketchum* v. *Duncan, supra,* and leaves the application of that case un-

**Ketchum* v. *Duncan* was relied on and followed by the Court of Appeals for the District of Columbia in *Lee* v. *Mitcham*, 98 F. (2d) 298, which presents a situation similar to that in the case at bar. The decision in that case on the point of assent cannot be reconciled with that in the instant one. In that case the court held there was a "purchase" of a note instead of "payment" where it was taken up without any actual notice to the holder that it was not to be discharged.

certain, but it is in apparent conflict with the decision of the Fifth Circuit in *Anderson* v. *Pennsylvania Hotel Co.*, 56 F. (2d) 980.

The Circuit Court, in its opinion in the present case, states (Rec. p. 112):

> "But we think that if the person making such a payment desires to exercise the option to treat the transaction as a purchase, he should manifest his intention to do so by some sort of notice to the coupon-holder, and he should disclose his intention at the time."

Such a requirement is something completely dehors the mortgage indenture but is implied by the court into the contract between the issuer and the bondholders. No such requirement of notice appeared in the indenture in the *Anderson* case, *supra*, and the court there granted parity to the bonds without requiring any proof of notice of intention to hold the bonds unsubordinated.

Furthermore, the *Anderson* case places the burden on the party opposing the claim of parity to show that, while some of his bonds were acquired by the paying agent, he held other bonds through to foreclosure and thereby would be harmed by a grant of parity to the paying agent. No such proof exists here. All the record shows (p. 31) is that—

> "Certain of the bonds acquired by American Bond & Mortgage Company and on which the plaintiff in this case asserts its rights were held at the time of such acquisition by persons who held other bonds of the same issue who later deposited these other bonds with the Committee."

All that the present respondents have proved, therefore, is that "certain" of the bondholders whose rights they have acquired will receive less if parity is accorded to the bonds

held by the petitioner. Moreover, there is absolutely nothing in the record to show that the "certain" bondholders suffered loss through postponement of foreclosure. They were quite content to take the paying agent's money and have never offered to return it. It did not appear that the properties fetched less on foreclosure than they would have fetched earlier. In the case of the Myles Standish the bid at the sale was the full amount of the indebtedness including the securities here in suit. It does appear that they will profit by parity being denied (they are the immediate recipients of the forfeiture), but that is a very different thing from a showing that they will suffer damage from parity being allowed. The decision of the Circuit Court of Appeals in denying parity to the petitioner in the absence of such proof of damage is in conflict with the decision of the Fifth Circuit in the *Anderson* case, *supra*. The existence of such a conflict, the petitioner asserts, further justifies the granting of the present petition for certiorari.

Turning to the applicable state cases, we again find the present decision of the First Circuit in irreconcilable conflict. In *Lyman* v. *Stevens*, 123 Conn. 591, the trustee under a corporate mortgage picked up matured bonds and coupons in pursuance of an indenture provision to the effect that the trustee might advance principal or interest not paid by the issuer and should thereupon to the extent of such advances be subrogated to the rights of the holders. This was done and the trustee was permitted to share in the security. While the court stated that the trustee (unlike the Mortgage Company here, an undoubted fiduciary) should have given notice that there was a default and that it proposed to seek subrogation for amounts advanced by it, it held that this was immaterial since it did not appear that the bondholders were in any way damaged by the trustee's failure to give such notice. As had been explained above in respect to the *Anderson* case, the requirement of proof

of damage marks a point of sharp conflict with the present decision.

Chicago Title & Trust Co. v. *Hoffberg*, 293 Ill. App. 290, 12 N.E. (2d) 230, is also irreconcilable with the present decision in that proof of ownership of other bonds and coupons by those objecting to parity was held essential.

The present decision, when viewed against the background of the prior judicial determinations on the subject which have been cited above, raises such sharp conflicts and leaves this branch of the law of corporate securities shrouded in such a mist of uncertainty that this Court, in the interest of promoting a uniformity of judicial decision and of clearly delimiting the rights and duties of those interested in or dealing with corporate securities, should grant the present petition.

III. The imposition of the forfeiture resulting from the decision below should be reviewed by this Court.

Although this Court in granting certiorari is properly concerned more with achieving uniformity of decision and practice than in correcting errors in particular decisions, miscarriage of justice must always be a pertinent and persuasive consideration. We present a grave miscarriage of justice on this record as an additional reason for granting the writ.

Bonds were sold by petitioner's predecessor, the Mortgage Company, to float wholly new ventures. Such "construction bonds" are notoriously a hazardous investment. They were conspicuously labelled "construction bonds" upon their face. They were issued under indentures which specifically provided that in the event of default by the issuer the Mortgage Company might purchase the bonds and coupons, hold them, and enforce them against the security. The Mortgage Company occupied no fiduciary

relationship which would disqualify it from making such a purchase.* There could be no possible objection, even had there been no indenture provisions, to a negotiated purchase and subsequent realization on the security. The issuer did default. The Mortgage Company advanced some $325,000 of its own money and took up the defaulted obligations. In so doing it acted in entire good faith, but it gave no notice that there was a default.† It did not intend to discharge or "pay" the obligations. The bondholders took its money quite happily. No offer has ever been made to return one penny of the money. It does not appear that any bondholder has suffered any damage by reason of this advance or would suffer any if parity is accorded to petitioner in the security. It does appear that all bondholders who took the Mortgage Company's money will necessarily profit by the transaction. Yet because the Mortgage Company failed to give notice that it intended to "purchase" rather than to donate its money and so to "pay," the Circuit Court of Appeals has enforced a forfeiture—and the cases are in equity.

Furthermore, this forfeiture has been enforced, not against the Mortgage Company itself, but against its creditors. The securities held by the petitioner, which the opinion of the Circuit Court of Appeals deprives of all value, it holds for the benefit of the creditors of the Mortgage Company. In *Lyman* v. *Stevens*, 123 Conn. 591, *supra*, a similar situation existed and was specially noticed by the

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*See *Hallett* v. *Moore*, 282 Mass. 380, and *Maryland Casualty Co.* v. *Moore*, 82 F. (2d) 189 (C.C.A. 1), which were cases in each of which endeavour was made to show identity between the trustee under the Pelham Hall mortgage and the Mortgage Company. In each case the endeavour was not successful.

†The District Judge in his opinion stated: "I have no doubt that the Mortgage Co., in financing these defaults, relied upon these provisions of the trust mortgages and believed it was incurring no risk in so doing" (Rec. p. 53).

court as an additional reason for refusing to impose a forfeiture.

On these facts we confidently assert that the petitioner has suffered an injustice. The question of law involved is one of general application in an important field of investment. An important point of practice is presented. We ask this Court to review the cases.

Respectfully submitted,

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